



MEMORANDUM

TO: HONORABLE MAYOR AND MEMBERS OF THE CITY COUNCIL
FROM: DENNIS McLEAN, DIRECTOR OF FINANCE & INFORMATION TECHNOLOGY
DATE: OCTOBER 1, 2013
SUBJECT: SCOPE OF SERVICES FOR REVIEW OF EMPLOYEE COMPENSATION
REVIEWED: CAROLYN LEHR, CITY MANAGER

Staff Coordinator: Kathryn Downs, Deputy Director of Finance & Information Technology

RECOMMENDATION

Recommendation of the City Council Ad-Hoc Subcommittee for 2013 Employee Compensation

1. Agreed upon review procedures of City Manager salary and benefits have been completed by the City's independent auditor for calendar year 2012 for an out-of-pocket cost of \$2,500. Direct Staff and the auditor to complete procedures for one additional calendar year (2009) for an additional out-of-pocket cost of \$2,250.
2. Direct Staff and the auditor to complete Phase 2 procedures, as defined in the attached Engagement Letter from the independent auditor (see attachment A), at a cost of \$5,000, plus an estimated \$2,500 one-time custom payroll system report cost (out-of-pocket costs totaling about \$7,500).
3. Direct Staff to return with a proposed budget adjustment for FY13-14 in the amount of about \$9,750.
4. Direct Staff to include the proposed auditor fee for Phase 2 procedures in annual draft budgets going forward (a discretionary expenditure of about \$5,000 each year).
5. Determine whether other review procedures should be defined and a proposal presented to City Council for approval.

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EXECUTIVE SUMMARY

The City Council Ad-Hoc Subcommittee for 2013 Employee Compensation ("City Council Subcommittee"), comprised of Mayor Brooks and Mayor Pro Tem Duhovic, expressed interest in requesting the City's independent auditor to conduct additional agreed upon review procedures related to employee compensation. Agreed upon review procedures of City Manager salary and benefits has been completed by the City's independent auditor for calendar year 2012. The results of the tests that have been completed are "clean" as described later in this Report.

Staff is requesting the City Council to determine whether additional test procedures should be completed. The City Council's alternatives include:

1. Do nothing further (actual out-of-pocket cost of \$2,500 to date).
2. Adopt the City Council Subcommittee recommendation to test the City Manager's compensation for calendar year 2009 at an out-of-pocket cost of \$2,250.
3. Direct Staff and the auditor to conduct Phase 2 procedures for calendar year 2013 at a cost of \$5,000, plus an estimated \$2,500 one-time custom payroll system report cost (out-of-pocket costs totaling about \$7,500).
4. Direct Staff to return with a proposed budget adjustment for FY13-14 in the amount of about \$9,750.
5. Include the proposed fee for Phase 2 procedures in the draft budget annually going forward (a discretionary expenditure of about \$5,000 each year).
6. Direct the City Council Subcommittee to define other procedures and present a proposal to the City Council.

BACKGROUND

In January 2013, the City received two separate requests for employee compensation records pursuant to the Public Records Act (PRA). Prior to receiving those requests, City Staff had posted extensive employee compensation information on the City's website including:

- Employee actual salary rates;
- Employee compensation information as requested by the California State Controller's Office (Medicare taxable income and certain City-paid benefit costs);
- The City Manager's employment contract and amendments approved by the City Council;
- Employee salary ranges approved by the City Council;
- Maximum employee health insurance payments approved by the City Council;
- A summary of benefits provided to full-time employees;
- Information regarding the City's employee pension plan, including the most recent actuarial valuation report from the California Public Employees Retirement System;
- The City's Personnel Rules; and

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- The Employee Handbook.

After completion of the employee compensation PRA requests, the City Council Subcommittee expressed an interest in requesting the City's independent auditor to conduct additional review procedures related to employee compensation. The purpose of the additional procedures established between the City Council Subcommittee and the auditor would be to demonstrate the City's compliance with its policies and procedures for employee compensation.

On August 8, 2013, the City Council Subcommittee met with Kevin Pulliam, the engagement partner of the City's independent audit firm, Vavrinek, Trine, Day & Co., LLP. Mayor Brooks was traveling and unable to attend. The Mayor Pro Tem met with Mr. Pulliam and worked through the scope and purpose for the auditor's "agreed upon procedures". Mr. Pulliam prepared an Engagement Letter with a \$7,500 fee proposal that was reviewed by Staff and signed by the City Manager (see Attachment A). The \$7,500 fee estimate for the agreed upon procedures for 12 months of payroll records is within the City Manager's purchasing authority.

On August 30, 2013, the City Council Subcommittee met with Staff to discuss the scope of the auditor's procedures and timelines for City Council consideration. The City Council Subcommittee was provided with a copy of the auditor's Engagement Letter that was authorized by the City Manager.

DISCUSSION

The agreed upon procedures have been defined and split into two phases described below (Phases 1 and 2). The procedures are outlined in the attached Engagement Letter.

Phase 1 – Test the City Manager's Compensation

The City Manager has stated in a public meeting and communicated to the City Council Subcommittee that she is very willing to have her compensation tested by an outside independent auditor since inception of her employment with the City. As such, the City Manager authorized the City's independent auditor to proceed with Phase 1 procedures for 12 months of payroll records (calendar year 2012) for a fee of \$2,500.

In addition to the fee charged by the City's auditor, the City will incur a significant amount of Staff time dedicated to this project as estimated below.

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Estimated Staff Hours for Phase 1 – Substantially Completed

Phase 1 Task	Hours Estimate
Meet with Mayor and Mayor Pro Tem	5.00
Review and sign engagement letter, and arrange logistics for auditor fieldwork	1.50
Furnish the auditor with employment contracts, personnel rules and other City policy documents and public records	1.00
Pull payroll records for calendar year 2012	2.00
Pull relevant accounts payable records for calendar year 2012	1.00
Answer auditor questions	2.00
Replace both payroll and accounts payable records after auditor fieldwork	1.00
Review auditor draft report	1.00
Prepare Staff Report to City Council, and management review	6.00
Estimated Staff Hours Phase 1 (for 12 months, substantially completed)	20.50

To facilitate the portion of the review that has been substantially completed, two tasks have been delayed: 1) preparation for the City's financial statement audit for FY12-13; and 2) the Staff Report for FY12-13 Continuing Appropriations (delayed from September 3rd agenda to September 17th).

Estimated Staff Hours for Phase 1 – Not Yet Completed

Phase 1 Task	Hours Estimate
Review and sign engagement letter, and arrange logistics for auditor fieldwork	1.50
Furnish the auditor with public records related to 2009 compensation	1.00
Pull payroll records for calendar year 2009	2.50
Pull relevant accounts payable records for calendar year 2009	1.00
Answer auditor questions	1.00
Replace both payroll and accounts payable records after auditor fieldwork	1.00
Review auditor draft report	1.00
Prepare Staff Report to City Council, and management review	6.00
Estimated Staff Hours Phase 1 (for 2009, not yet completed)	15.00

To facilitate the Phase 1 procedures that have not yet been completed, Staff expects that other projects will be delayed.

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Results of Phase 1 – Substantially Completed

The auditor conducted fieldwork on September 4th and 5th, and has issued a report (see Attachment B). The auditor's procedures, outlined in the auditor's report, were very thorough and detailed. For example, the procedures to review payments to the City Manager (e.g. expense reimbursements) from the disbursement system (warrant register) included a review of all disbursements for calendar 2012 to ensure no payments were missed. The report indicates that no exceptions were noted from Staff's compliance with the City's policies and procedures in administering the compensation provisions of the City Manager's employment agreement during 2012 (this is a "clean" report).

Phase 2 – Prepare New Employee Compensation Schedule and Auditor Tests

Staff would prepare a schedule of all categories of employee compensation for all individuals issued a W-2 from the City for 2013. The auditor would trace amounts to supporting documentation for a sample size of 20 employees to include all management employees. Neither Staff nor the auditor have begun Phase 2 procedures. The out-of-pocket cost is expected to be about \$5,000 for the auditor's services plus \$2,500 for a custom report developed by the City's payroll processing company (ADP). If City Council elects to move forward with Phase 2 procedures, the independent auditor expects the work could be done and a report issued by February 2014.

Staff has attached a template for the schedule of employee compensation to be prepared as part of Phase 2 procedures (see Attachment C). The template is similar to a schedule that has been prepared by Ken Dyda as part of his January 2012 and January 2013 Public Records Act requests. Mayor Pro Tem Duhovic also supports preparation of the proposed schedule.

As required by the California State Controller, the City prepares a schedule of employee compensation that reflects annual taxable income for every employee who received a W-2 for a calendar year, and posts the schedule to the City's website (see Attachment C). The primary benefits of the State Controller's schedule include public disclosure and comparability with other cities. The primary weakness of the State Controller's schedule is the fact that it lists taxable compensation, net of employee's voluntary contributions to benefit plans, and not gross compensation.

There is no state or other legal requirement to prepare the schedule that is part of Phase 2 procedures (Attachment B). As such, it is possible that a member of the public could attempt to compare employee compensation data included within the new schedule to the State Controller's schedule for other cities, creating an apples to oranges comparison. Staff believes that the schedule proposed as a part of Phase 2 would not improve financial management of the City, nor does it seem like a useful tool for the City Council to make policy decisions. The usefulness of the new schedule would be measured as the degree to which City Council sees value in additional transparency or as a response to residents who have made inquiries. However, Staff believes this usefulness would be tempered by the

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potential for confusion related to two different employee compensation schedules.

Estimated Staff Hours for Phase 2 – Not Yet Completed

Phase 2 Task	Hours Estimate
Define fields for custom ADP report, negotiate ADP service, review draft ADP report for accuracy	8.00
Use ADP report to create Schedule as defined in Phase 2, review for accuracy	6.00
Arrange logistics for auditor fieldwork	1.00
Pull payroll records for calendar year 2013	4.00
Pull relevant accounts payable records for 2013	2.00
Answer auditor questions	4.00
Replace both payroll and accounts payable records after auditor fieldwork	2.00
Review auditor draft report	2.00
Prepare Staff Report to City Council, and management review	8.00
Estimated Staff Hours Phase 2 (for 12 months, not yet completed)	37.00

To facilitate the Phase 2 procedures that have not yet been completed, Staff expects that other projects will be delayed, including recognition of the City's loan to the former redevelopment agency as an enforceable obligation.

Other Additional Procedures Not Yet Defined

Other procedures may include a review of employee leave time, overtime, cashing in unused vacation time, employee expense reports, and legal services billings. If the City Council elects to move forward with other procedures, the 2013 Employee Compensation Subcommittee would define procedures and develop a proposal for City Council consideration by February 2014, which would include a cost estimate.

FISCAL IMPACT

The Finance program budget in the General Fund for professional services can absorb the audit fee of \$2,500 for procedures that have already been completed. If the City Council directs Staff to move forward with the City Council Subcommittee's recommendation, Staff will return with a proposed budget adjustment of \$9,750 in the City's General Fund.

Attachments:

- A – Signed Engagement Letter
- B – Auditor's Report on Agreed Upon Procedures
- C – Template for Schedule of Employee Compensation



Vavrinek, Trine, Day & Co., LLP
 Certified Public Accountants

VALUE THE DIFFERENCE

August 15, 2013

City Council
 City of Rancho Palos Verdes, California

We are pleased to confirm our understanding of the nature and limitations of the services we are to provide for the City of Rancho Palos Verdes (the City).

We will apply the agreed-upon procedures which the City Council has specified, listed in the attached schedule, to the City's payroll records and benefit documentation. This engagement is solely to assist the City in determining that payroll, paid benefits and earned benefits agree, for the sample noted, to the underlying supporting documentation. Our engagement to apply agreed-upon procedures will be conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of those parties specified in the report. Consequently, we make no representation regarding the sufficiency of the procedures described in the attached schedule either for the purpose for which this report has been requested or for any other purpose. If, for any reason, we are unable to complete the procedures, we will describe any restrictions on the performance of the procedures in our report, or will not issue a report as a result of this engagement.

Because the agreed-upon procedures listed in the attached schedule do not constitute an examination, we will not express an opinion on the balance, amounts, or on compliance with applicable policies, regulations, requirements or statutes. In addition, we have no obligation to perform any procedures beyond those listed in the attached schedule.

We will submit a report listing the procedures performed and our findings. This report is intended solely for the use of the City Council, and should not be used by anyone other than these specified parties. Our report will contain a paragraph indicating that had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

The City is responsible for compliance with all policies, regulations, requirements, and statutes and is responsible for selecting the criteria for testing and for determining that such criteria are appropriate for your purposes.

Kevin Pulliam is the engagement partner and is responsible for supervising the engagement and signing the report or authorizing another individual to sign it.

We plan to begin our procedures during September 2013 and, unless unforeseeable problems are encountered, the engagement should be completed by (as detailed below in the Scope of Work): Phase I – October 10, 2013; Phase II – January 31, 2014. At the conclusion of our engagement, we will require a representation letter from management that, among other things, will confirm management's responsibility for the compliance with all applicable policies and statutes in accordance with those standards.

We estimate that our fees for these services will be \$7,500 (estimated at \$2,500 for Phase I and \$5,000 for Phase II). The fee estimate is based on anticipated cooperation from your personnel and the assumption that unexpected circumstances will not be encountered during the engagement. These fees are also based upon the assumption that the City will have all of the detail ready for each sample selected for the specified procedures noted in the Scope of Work for the team upon arrival (a prepared by client listing (PBC) will be provided a minimum of 2 weeks before scheduled fieldwork). If significant additional time is necessary, we will discuss it with you and arrive at a new fee estimate before we incur the additional costs.

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We appreciate the opportunity to assist you and believe this letter accurately summarizes the significant terms of our engagement. If you have any questions, please let us know. If you agree with the terms of our engagement as described in this letter, please sign the enclosed copy and return it to us. If the need for additional procedures arises, our agreement with you will need to be revised. It is customary for us to enumerate these revisions in an addendum to this letter. If additional specified parties of the report are added, we will require that they acknowledge in writing their responsibility for the sufficiency of procedures.

Very truly yours,



Kevin T. Pulliam, Partner
Vavrinek, Trine, Day & Co., LLP

KTP:gbl

Attachment

RESPONSE:

This letter correctly sets forth the understanding of the City of Rancho Palos Verdes.

By: Carolyn Zehr

Title: CITY MANAGER

Date: 8-29-13

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Scope of Work

Perform an agreed upon procedures engagement (AUP) to assist the City in determining that the payroll, paid benefits and earned benefits agree, for the sample noted, to the underlying supporting documentation. The work will be performed in phases as noted below:

Procedures:

Phase I:

1. For the City Manager's contract perform the following:
 - a. Trace all payroll, city paid benefits, earned benefits as noted in procedure #2 from the City Manager's contract to the actual payment/earned benefit supporting documentation.
 - b. Trace all payroll, city paid benefits, earned benefits from the City's detailed records into the City Manager contract.
 - c. Trace all wages to the W-2 filing.
 - d. Trace all other payments through the City's disbursement system, if any, and review for proper approval, etc. in accordance with City policy.

Phase II:

2. Trace applicable information on the attached worksheet (prepared by the City) to applicable Internal Revenue Service and Franchise Tax Board filings.
3. Select a sample of the following for a total sample of twenty (20);
 - a. all senior management,
 - b. and approximately ten (10) percent from each of the following categories:
 - i. full time personnel
 - ii. part time personnel
 - iii. City Council
 - iv. City Commissioners.

For the selected sample trace the following to current published policies and procedures including but not limited to: City personnel records, contracts if applicable, policies, and other supporting documentation:

1. Payroll:
 - a. Annual salary
 - b. Overtime
 - c. Auto allowance
 - d. Bonus
 - e. Vacation buyout
 - f. Health insurance in-lieu

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Phase II, (Continued):

2. City Paid Benefit Costs:

- a. Pension benefits
- b. Insurance – including but not limited to: Medical, Vision, Dental
- c. Medicare
- d. Retirement Health Savings Account Contribution
- e. Deferred Comp

3. Benefits – Earned Hours Only:

- a. Wellness
- b. Admin Leave
- c. Sick Leave
- d. Holidays
- e. Vacation
- f. Comp Time

CITY OF RANCHO PALOS VERDES

**Independent Accountants' Report on
Agreed-Upon Procedures Performed
with Respect to the City Manager's Employment Contract**

For the Calendar year ended December 31, 2012



**INDEPENDENT ACCOUNTANTS' REPORT
ON APPLYING AGREED-UPON PROCEDURES PERFORMED
WITH RESPECT TO THE CITY MANAGER'S EMPLOYMENT CONTRACT**

City Council
City of Rancho Palos Verdes

We have performed the procedures enumerated below, which were agreed to by the City of Rancho Palos Verdes (City) solely to assist you with respect to your evaluation of selected provisions of the City Manager's employment contract for the calendar year ended December 31, 2012. The City's management is responsible for the execution of the provisions contained in the City Manager's employment contract. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the City. Consequently, we make no representation regarding the sufficiency of the procedures described below, either for the purpose for which this report has been requested, or for any other purpose.

The procedures performed and the results of those procedures were as follows:

1. For the City Manager's contract perform the following:

- a. Trace all payroll, city paid benefits, earned benefits from the City Manager's contract to the actual payment/earned benefit supporting documentation

Result: We traced all payroll, city paid benefits, earned benefits from the City Manager's contract to the actual payment/earned benefit supporting documentation. No exceptions were noted.

- b. Trace all payroll, city paid benefits, earned benefits from the City's detailed records into the City Manager contract

Result: We traced all payroll, city paid benefits, earned benefits from the City's detailed records to the City Manager's contract. No exceptions were noted.

- c. Trace all wages to the W-2 filing

Result: We traced all wages to the W-2 filing. No exceptions were noted.

- d. Trace all other payments through the City's disbursement system, if any, and review for proper approval, etc. in accordance with City policy

Result: We traced all other payments through the City's disbursement system and reviewed for proper approval in accordance with City policy. No exceptions were noted.

Attachment B

We were not engaged to, and did not, conduct an audit, the objective of which would be the expression of an opinion on the City, related internal control, compliance with government code, or elements, accounts or items specified above. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the City Council and management of the City and is not intended to be, and should not be, used by anyone other than those specified parties.

Vawrmile, Tami, Day, Co., LLP

Rancho Cucamonga, California
September 9, 2013

Employee Name	Title	2013 Actual City Paid				2013 City Contributions To:										Total 2013 City Cost	2013 Hours Earned					Comp Time In lieu of Paid OT
		Salary	Auto	Over Time	Bonus	Vacation Buy-Out	Subtotal Gross Income	Pension	Medical Insurance	Vis/Dent Insurance	Life Insurance	AD & D Insurance	Long Term Disability	Retiree Health Savings	Deferred Comp	Subtotal Benefits	Wellness	Admin Leave	Sick	Vaca	Holiday	
Employee 1																						
Employee 2																						
Employee 3																						